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CC:EL:GL:ICPlucinski
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Acting National Director, Submission Processing T:S

Chief, Branch 2 (General Litigation) CC:EL:GL:Br2

Significant Service Center Advice: Remittances Received
with Form 940

This responds to your request for advice, dated February 13, 1997, regarding the legality of "overstamping" remittances received with Form 940, Employer's Annual Federal Unemployment Tax Return, made payable to a state agency.

Disclosure Statement

Unless specifically marked "Acknowledged Significant Advice, May be Disseminated" above, this memorandum is not to be circulated or disseminated. This document may contain confidential information subject to the attorney-client and deliberative process privilege. Therefore, this document shall not be disclosed beyond the Office or individual(s) who originated the question discussed herein and are working the matter with the requisite "need to know." In no event shall it be disclosed to taxpayers or their representative.

Issue

Whether remittances received with Form 940, Employer's Annual Federal Unemployment Tax Return, but payable to a state agency may be "overstamped" with the words "Internal Revenue Service" and processed as payment for taxes due on Form 940.

Conclusion

We conclude that remittances made payable to a state agency should not be "overstamped" with the words "Internal Revenue Service" and processed as payment for taxes due as

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reported on the Form 940.

Facts

Form 940, Employer's Annual Federal Unemployment Tax Return, provides that a check or money order for the balance due reported on Form 940 should be made payable to the Internal Revenue Service. A number of remittances received in the service centers with the Form 940, however, are made payable to a state agency, such as a State Treasurer, State Department of Revenue, or State Unemployment Agency, rather than to the Internal Revenue Service. These remittances are generally written for the correct amount. Nonetheless, the service centers are returning these checks and/or money orders to the taxpayer because state agencies are not considered an acceptable payee under the current Internal Revenue Manual procedures.

Discussion

Internal Revenue Manual ("IRM") 38(43)3.2 governs the perfection of remittances received by service centers. IRM 38(43)3.2(1) lists the types of remittances which are subject to these procedures. These remittances include: personal checks, money orders, cashier checks, business checks, certified checks, voucher checks, and draft type checks. According to paragraph (3) of IRM 38(43)3.2(3), if a payee on a remittance is the "IRS" only, "cash," or if the payee line is left blank, the payee line must be overstamped with the words "Internal Revenue Service" before the remittance can be processed. IRM 38(43)3.2(3). See also IRM 592(12).2(d)1. Paragraph (5) governs perfection of remittances not payable to the "IRS." This paragraph provides in relevant part:

If remittance is not endorsed to the Internal Revenue Service or one of the acceptable payees listed in Exhibit 38(43)0-4, return remittance to the taxpayer

IRM 38(43)3.2(5)(a). See also IRM 592(12).2(d). Because a state agency is not one of the acceptable payees, the service centers are currently unable to process remittances received with Form 940 but payable to a state agency, unless the check and/or money order received with Form 940 is endorsed to the Internal Revenue Service.

In our previous memorandum, dated May 24, 1993, addressing the Service's "overstamping" procedure, we concluded that "if the payee of the taxpayer's check is not the Service, the Social Security Administration (SSA), FICA, or another Governmental agency, and the payee has not

endorsed the check, we believe that the check should be returned to the taxpayer as an unacceptable payment." See IRM 592(12).2(1)(d)8. We believe this is still the correct approach.

Revised Article 3 of the Uniform Commercial Code ("U.C.C.") governs negotiable instruments. ¹There are two categories of negotiable instruments: drafts and notes. The term "draft" includes a check, cashier's check, teller's check, and certain types of money orders. See U.C.C. § 3-104(f). ²

The Revised Uniform Commercial Code defines a check as an order to pay a fixed amount of money, drawn on a bank, and payable on demand. U.C.C. § 3-104. It must be payable either to bearer or to order of a specific person or entity. ³ If a check is payable to bearer it can be negotiated by delivery alone. If it is made payable to order of a specific person or entity, however, it cannot be negotiated without the indorsement of the person or entity identified on the payee line. U.C.C. § 3-201(b).

The identity of a person or entity to whom the check is payable is determined by the intent of the issuer of the check. U.C.C. § 3-110. Thus, a check is payable to the person or entity intended by the signer of the check even if that person or entity is identified by a name that is not that of the intended person or entity. See Hartford Accident & Indem. Co. v. American Express Co., 544 N.Y.S.2d 573 (1989). Accord Gino's of Capri v. Chemical Bank, 592 N.Y.S.2d 682 (1993). ⁴ For example, a taxpayer intends to pay a person known to the taxpayer as John Smith. In fact

¹ Article 3 (formerly Commercial Paper, now Negotiable Instruments) was revised in 1990, and approved by the National Conference of Commissioners on Uniform State Laws and the American Law Institute in 1990. Since then, 42 states have adopted the Revised Article 3.

² All references to the U.C.C. are to the Revised Article 3, unless otherwise indicated.

³ A check written for "cash," for example, is payable to bearer. U.C.C. § 3-109(a).

⁴ Both cases were decided under the Pre-1990 version of Article 3. That version did not contain the explicit language of the current section 3-110.

that person's name is John Jones, or some other entirely different name. If the check identifies the payee as John Smith, it is nevertheless payable to John Jones because John Jones is the person intended by the taxpayer. See notes to U.C.C. § 3-110.

While majority of remittances received with a processable Form 940 are intended for the Internal Revenue Service, even though some are made payable to a state agency, we believe that the Service should not "overstamp" these remittances with the words "Internal Revenue Service," but should return the remittance to the taxpayer. The reasons for this conclusion are as follows. First, not all states have adopted the Revised Article 3 and those that have adopted it may have slightly changed the language of the provision. In order to implement an "overstamping" procedures that would not subject the Service to undue hazards of litigation over small amount of tax due, a review of each state law would be necessary to produce a list of states where checks could be "overstamped." Service center employees who were processing these checks would then be required to determine which state law would govern and consult the list to ascertain whether a particular check could be "overstamped." This procedure would likely be more cumbersome and costly than returning the check to the taxpayer to be correctly addressed.

In addition, the provision of the U.C.C. that would support "overstamping" is relatively new, and there is no case law interpreting the types of facts that would be sufficient to establish that the intent of the payor/taxpayer was to make the check payable to the Service. As a result, banks may be unwilling to honor checks and money orders that have altered payees because they are concerned about their liability if a customer/taxpayer challenges the bank's decision to pay the check to the Service.⁵ If that were to happen, the Service would still have to return the check to the taxpayer to be properly addressed.

Based on the above it is our position that remittances received with Form 940, Employer's Annual Federal Unemployment Tax Return, payable to a state agency may not

⁵ While we agree with your assessment that majority of the remittances received with Form 940 are intended as payment of unemployment tax due as reported on Form 940, we suspect that some of these remittances are in fact intended as payment of state tax obligations.

be "overstamped" and processed as payment for taxes due on Form 940, but must be returned to the taxpayer in accordance with IRM 38(43)3.2(5)(a).

This matter has been assigned to Inga C. Plucinski, who may be reached at (202) 622-3620, if you have any comments or questions regarding this matter.

KATHRYN A. ZUBA

cc: Executive Office for Service Center Operations